

**Before the Federal Communications Commission
Washington, DC 20554**

In the Matter of:)	
)	
Schools and Libraries Universal)	CC Docket No. 02-6
Service Support Mechanism)	

**I. COMMENTS SUBMITTED BY
THE OFFICE OF INFORMATION TECHNOLOGY SERVICES
OF NORTH CAROLINA
IN RESPONSE TO THE
RELEASED JANUARY 25, 2002
NOTICE OF PROPOSED RULEMAKING & ORDER**

I. Introduction

The Office of Information Technology Services (ITS) respectfully submits these comments in the above referenced proceeding. ITS is a State Telecommunications Network (STN) and serves as a billed entity within the E-Rate program. At present ITS services approximately 65,000 lines. These comments are directed to telecommunications services, and not to issues of internet access or internal connections support. ITS commends the Federal Communications Commission (Commission) for its ongoing commitment to expand universal service of telecommunications services by supporting the Universal Service Program for Schools and Libraries, often referred to as the E-Rate Program (E-Rate).

ITS personnel participate in National Association of State Telecommunications Directors (NASTD) and the Council of Chief State School Officers (CCSSO), comprised of state E-rate coordinators. NASTD and CCSSO members have intimate knowledge of the E-rate program. CCSSO E-Rate coordinators aid their respective school districts with their E-rate applications, and, in some instances, are responsible for state consortia applications. This group regularly works with the Universal Service Administrative Company's Schools and Libraries Division ("Administrator"), and has a particularly good grasp of the program's history and intent. ITS' comments reflect specific concerns for its position as a STN and concur in some of the CCSSO comments.

The E-rate Program has successfully spurred connectivity across the nation, especially in K-12 schools and districts in poor and rural areas. North Carolina has 117 school districts in 100 counties, and 85 of these counties are considered rural. Hence, the E-Rate program has high importance for ITS, and the schools and libraries served. The program's primary focus should remain with these schools and libraries, assisting them to complete their network infrastructure and allow on-going maintenance.

The Commission requested comments on specific issues and in the general program administration in the Notice of Proposed Rulemaking and Order (NPRM), to improve E-Rate operations, ensure equitable distribution of program funds, and prevent fraud, waste and abuse. We appreciate the opportunity to provide a perspective as a unique STN and consortium comprising schools we serve.

II. Summary of Comments

A. 1. ITS supports amending the eligible services list to focus on functionality, rather than specific products or services.

A. 5. As an State Telecommunications Network (STN), ITS has the ability to achieve significantly discounted telecommunications service rates compared with typical tariff rates paid by schools and libraries. ITS provides telecommunications services to approximately 65,000 clients; comprising state agencies, universities, schools, local governments and other governmental units. ITS pricing, based on its mandated cost recovery model, constitutes only 60%-70% of tariff pricing for services billed to ITS school and Library clients. Based on sampling 25% of ITS' school clients, the Administrator could realize annualized program savings of \$891,980 and schools in the sample population could realize savings of \$372,352; hence total savings may constitute a fourfold increase over the sample.

C. 1,2. ITS supports extending the appeals period to 60 days. ITS also supports rolling unused funds forward when released from appeal reserves.

III. Comments

A. Application Process

1. Eligible Services

Paragraphs 13-14. Attempts to discern the eligibility or non-eligibility of individual technological components of telecommunications and advanced services has limited school-based choices for technology infrastructure. Experience and technical advancement have broadened the list of eligible services. As the list has become more product specific, schools have been forced to choose technological solutions that are not as cost effective or current, but meet the guidelines of the program. For example, leasing technology from a telecommunications provider offers greater assurance that the service will be eligible for discount; albeit subject to ineligible express or hidden financing charges. Leasing wireline equipment through an eligible telecommunications carrier, while potentially more expensive over the longer term, is employed frequently because the E-rate program discounts that solution.

Smaller districts, particularly rural districts with few technology staff, if any, are disadvantaged by the complexities of the E-Rate process and unpublished lists of eligible services. These smaller districts often lack the personnel and economic resources to seek and achieve funding from the program. The level of sophistication required to decipher the school district's phone bills and determine which phone lines are eligible and which are not require more energy than the program is worth to such a district. This difficulty results in a need for centralizing administration with experienced and knowledgeable persons to achieve, or maximize, administrative efficiencies. This has led some districts to outsource the application process to contractors, and compensate the contractors with contingency fees. These fees may comprise 30% of the applicant's reimbursement. The current rules may not prohibit such activity, but the economic impact on schools, libraries, and the Administrator cannot be within the original intent of E-Rate.

Functionality is the most important principle governing the eligibility of services and products. We do not favor a specific list of approved products because specific products may be used for a variety of functions, comprising eligible and ineligible products and services. Schools and libraries have difficulty discerning whether a particular product or service is eligible by referencing the current eligible services list, because functionality and scope of the products or services must be used in procurement evaluations, but are not used in the eligible services list.

The General Accounting Office reported that the Administrator utilizes a list of more than 750 eligible items and services during the application review process as a result of General Accounting Office recommended improvements. (*Schools and Libraries Program: Application and Invoice Review Procedures Need Strengthening*, GAO 01-105, Page 19) The CCSSO reports that a Freedom of Information Act request for this list was denied. However, we understand that the list addresses the great majority of items current applicants use. This list is not shared with applicants in order to assure that there is no competitive advantage over products that are unknown, new or are offered by smaller providers that are infrequently used. The eligible services list should not be restrictive since that would violate the program tenet of competitive neutrality. Applicants should be given the ability to reference items not on the list in the application process and, if requested, provide defined documentation to support the item's eligibility.

While ITS appreciates the Administrator's interest in maintaining competitive neutrality by keeping the list private, this decision increases program costs associated with program review. It also negatively affects procurement efforts. As North Carolina's Information Technology (IT) procurement agency, ITS employs "best value procurement", focusing on the total costs of ownership rather than simply the lowest pricing. This allows procurement of IT goods and services at the most attractive overall costs while ensuring compatibility with existing and planned technology infrastructure. ITS therefore suggests compilation of an eligible services list based on function rather than specific products. Alternatively, the complete individual products and services list used by the Administrator should be made public.

5. Consortia

In Paragraphs 26-28, the Commission requests guidance to clarify that only ineligible private sector members seeking services as part of a consortium with eligible members are prohibited from obtaining below-tariffed rates from providers that offer tariffed services. The Commission also requests comment on whether the proposed rule change would increase or decrease administrative costs, and whether costs would outweigh the benefits of the change.

ITS commends the Commission on its decision to clarify this portion of the regulations and supports the change. ITS operates in precisely this manner under its legislation. Currently, the Administrator has extensive consortia cost allocation rules. These rules can accommodate the clarification without significant additional administrative burden.

In Paragraph 32, the Commission requests comments regarding additional modifications or suggestions to clarify, change or re-organize other rules and requirements relating to consortia. We provide additional comments here to assist the Commission in its efforts, and note that our comments are limited to telecommunications services. ITS has, perhaps, taken some liberty in providing an extensive response regarding STNs, and particularly our operations as a billed entity for telecommunications services.

Summary: As an STN, ITS has the ability to achieve significantly discounted telecommunications service rates compared with typical tariff rates paid by schools and libraries. ITS pricing constitutes only 60%-70% of tariff pricing from service providers for the same services to ITS school and Library clients. ITS sampled school clients and determined that the Administrator could realize annualized program savings of \$891,980 and schools in the sample population could realize savings of \$372,352. ITS does not receive appropriations from the NC General Assembly. We are statutorily required to operate under a cost recovery model by pro-rating costs for services proportionately across our client base. However, when pro-rated service recovery costs are excluded from sums submitted for reimbursement, schools and libraries actually have disincentives to participate in the E-Rate program. Further detail is provided below.

The Washington State Department of Information Services sought recognition of their STN costs as a class of advanced services eligible for Universal Service support (CC Docket No. 96-45, FCC 99-268, rel. date October 8, 1999). Their request was denied. This comment does not question the Commission's conclusions on the rationale and argument presented by Washington. However, after several year's operations, it is now possible to review funding eligibility and the operation of STNs as consortia in a more didactic manner.

The role of consortium leader is thrust upon ITS by 47 CFR 54.520(a)(3); wherein it states, "[i]n the case of a consortium, the billed entity is the lead member of the consortium", and relies upon 47 CFR 54.500 for the definition of "billed entity". ITS serves as the billed entity for the telecommunications contracts which it procures. ITS

provides billing administration services and additional services to its clients. ITS pricing from the service providers includes the regulatory fees and the line circuit; typical services and service provider costs are not included. ITS provides the same services typically provided by service providers; e.g. technical assistance, account analysis, service and equipment evaluation, planning, on site service and other similar services. These costs are incorporated into the bill sent to the service recipient, e.g. state agencies, local governmental units, state universities, schools or libraries. ITS billings are not used to subsidize other operations, nor other agencies.

ITS compiled statistics exemplifying the significant savings that may be achieved by STNs. For ease of data analysis, we collected information from 29 school districts that lie within the service area of a single underlying local service provider. These districts have E-Rate discounts ranging from 49% to 90%, with a mean of 73%; and total lines ranging from 35 to 580, with a mean of 185. The total monthly amount supported by universal service under tariff is \$170,943; if ITS bills were eligible this amount would be \$96,611; and the resulting monthly savings would be \$74,332. Annualized program savings would be \$891,980, or 43.5% in universal service support. Annualized savings for the schools in our sample would be \$371,352. As mentioned above, North Carolina has 117 school districts. Extrapolation of these figures demonstrates savings that may reach \$3,075,793 for the Administrator and \$1,280,524 for North Carolina's schools. Although precise figures may vary due to E-Rate discounts and other factors, these savings clearly benefit North Carolina schools and libraries by lowering their overall expenditures, and the program as a whole through cost savings and administrative economies.

The Commission cited certain program policies recognizing advantages for consortia in its decision denying funding for the Central Minnesota Computing Center (CMCC) (CC Docket 96-45, 97-21, DA 01-776, rel. date March 29, 2001). The Commission stated, "[w]here schools and libraries choose to apply as a consortium to obtain the resulting advantages, the consortium must be prepared to accept the associated burdens as well", (Id. at para. 12). This conclusion appears reasonable upon its face; however, it necessarily relies upon a presumption that costs of the consortium, together with costs of the service, will exceed the tariff costs from the underlying common carrier. Such a presumption presupposes that some of the recognized consortium advantages cannot achieve greater cost efficiencies than provided through service providers' tariff billing. This foundation is flawed. The Commission also found that STNs could not be classified as "common carriers" and therefore were not eligible for direct reimbursement (*Fourth Order on Reconsideration* 13 FCC Rcd 5424 at para. 182-9).

Advantages of consortia are presented as: (1) attracting competitors and negotiating lower prices by aggregating demand; (2) improving efficiency by consolidating services; and (3) reducing costs by sharing network infrastructure, knowledge, facilities and technical staff. (CC Docket 96-45, 97-21, DA 01-776 at para. 12, footnote 39) ITS observes that (3) may be more appropriate for discussion with internet access or internal connections in the context of STNs such as North Carolina. ITS further observes that (1) and (2) logically follow from the Fourth Reconsideration Order (13 FCC Rcd 5318, para.

183). The Commission's conclusions in this matter are supported by ITS' experience in aggregating demand and negotiating pricing in a competitive environment. As shown above, ITS pricing, based upon its mandated cost recovery model, constitutes only 60%-70% of tariff pricing for services billed to ITS school and Library clients.

The terms "telecommunications provider" or "common carrier" discussed in the Order should receive further consideration when applied to STNs. The rationale employed in the Iowa Communications Network (ICN) matter (CC Docket No. 96-45, FCC 00-449, rel. date Dec. 26, 2000) finding ICN within the definitions of "common carrier" and therefore "telecommunications provider" seems inapposite to ITS; but ITS finds this decision instructive. Unlike ICN, ITS does not own the network used to provide telecommunications services for voice. ICN met the definition of "common carrier", and therefore "telecommunications provider" based, in part, on its ownership of the network. Most STNs do not meet this definition because they operate as state agency aggregators (although not telecommunications aggregators as defined in 47 USC 226) that procure telecommunications services through competitive bidding for master contracts. The ICN decision recognizes that "common carrier" status does not always mean that services are provided to an unrestricted population. ICN's clients are limited to public and private agencies by state law. Hence, the ICN decision teaches that if the service population is circumscribed by state legislation, and the eligible services are provided to all members of said population seeking services, the "public offering" requirement of "telecommunications services" as defined in 47 USC 153(46) may include an entity such as ICN.

ITS, however, cannot seek classification as a carrier without violation of another statute (NCGS §147-33.92). Therein, ITS is prohibited from taking any action that may cause it to be considered as a utility, and subject to regulation by the state utilities commission. STNs such as ITS and eligible client agencies are then placed on the horns of a dilemma. The Commission's interpretation and application of 47 USC 254(h) with respect to STNs creates an economic paradigm that opposes the demand aggregation advantages inherent in STN operations. Schools and libraries electing to secure telecommunications services through ITS, however, face direct and indirect economic dilemmas. Although ITS pricing is quite favorable, two significant issues provide a disincentive for the schools to lower costs.

- First, ITS administrative cost recovery model is not permitted support from Universal Service. This means that schools and libraries must engage in a prospective economic analysis to compare E-Rate program discounts or reimbursements under differing contracts, with the resulting decision most often resulting in greater expense to the schools, libraries, and the program.
- Second, in recognition of the first issue, procurements for a local School or Library are not truly competitive due to issues associated with lack of demand aggregation, underlying service providers, and generally with lesser acumen in the procurement process.

ITS has two principle functions relevant to this matter. The first comprises provision of telecommunications services as described in NCGS §§147-33.91, 147-733.92. The second comprises procurement of all information technology (including telecommunications services) for state agencies; see NCGS §§147-33.82, 147-33.95. Schools and libraries are eligible to purchase telecommunications services through ITS, but are not required to do so. ITS operations compare favorably with the Commission's prior findings (Fourth Reconsideration Order, 13 FCC Rcd at 5427, para. 164-74).

North Carolina, like some other states operating a cost recovery STN, operates within a statutory framework that offers opportunity to its customers for cost savings; and offers opportunities to the E-Rate program for cost savings and administrative efficiency. Salient attributes are:

- The NC STN was created prior to the E-Rate program pursuant to state statute;
- It operates on a state mandated cost recovery system in which all customers are billed, pro-rata, for the overhead costs of the agency;
- Rate determination and cost recovery are determined by an independent body, the Information Resources Management Council (IRMC), whose members comprise representatives from multiple state agencies, private enterprise and the citizenry;
- ITS provides procurement services of all information technology (including telecommunications services) for state agencies through best value competitive bidding;
- Schools and libraries may, but are not required to, purchase telecommunications services through ITS contracts.

ITS therefore suggests consideration of rule changes recognizing specific benefits of STNs that address the two dilemmas posed above, and that benefit the E-Rate program. The Commission previously noted its broad authority under 47 USC 254(h)(2), "to enhance access to advanced telecommunications and information services, constrained only by the concepts of competitive neutrality, technical feasibility, and economic reasonableness" (Order, 12 FCC Rcd 9086). Universal Service, like any other cost-shifting paradigm, must seek the greatest dissemination of funds across eligible participants. ITS submits that the economic sampling presented above presents a compelling argument supporting modifications to recognize STN billings as eligible for reimbursement. We advocate modification, but with protections against waste, fraud and abuse. An STN must offer assurances of cost effective and responsible management. North Carolina accomplishes this by:

- NCGS §147-33.88 ITS rates incorporate cost recovery measures as required by statute. Rates are established based upon a budget

presented to a public oversight body (the IRMC), incorporated into the Governor's budget (Governor is the budget director under the NC Constitution), and submitted for approval to the NC General Assembly.

- NCGS §147-33.91-92 ITS must provide telecommunications services, to executive state agencies; while other governmental units such as state universities, local governments, schools and libraries may use ITS contracts at their option. ITS services include those customer services normally provided by telecommunications service providers.
- NCGS §§147-33.82, 147-33.95 ITS is the state's procurement agency for information technologies, including telecommunications services, and operates with a more extensive professional and technical staff than affordable by school districts or libraries.

Further, ITS does not seek abrogation of general conclusions disallowing direct reimbursement of STNs, but rather, recognition that the data now known from STN operations demonstrates the magnitude of savings and efficiencies support allowing schools and libraries reimbursement for the total bills submitted by STNs. Secondly, that administrative burdens for the Administrator, the STN and the participating schools and libraries will be substantially relieved by adoption of ITS' recommendations.

ITS proposes that the Commission require assurances as identified hereinabove for STNs, and accept a state statutory or regulatory framework as evidence of such assurances. Further, that the Commission may require STNs to present aggregated cost savings reports consistent with the manner in which costs for school and library districts are presented for reimbursement or discount. ITS supports establishing a price differential between the eligible costs from an underlying service provider, and STN billings, as this requirement will serve goals of competitiveness in bidding, and reducing potential for waste, fraud and abuse. We propose permitting schools and libraries applicable discounts or reimbursement for STN billings when such billings are not more than 90% of the tariff costs for the same services provided by the underlying service provider(s). This requirement serves to drive costs down. This is a much more competitive tool than bidding by single school districts; especially when only one or two service providers operate in the district, or when the business offered by a single school district is too small to attract competitive bids.

From the foregoing, one must note that there is no change in funding to the underlying carriers. This is apposite pursuant to the Commission's analysis in the Fourth Order on Reconsideration, 13 FCC Rcd at para. 198. Further, the Commission concluded that the discount applied should be applied to the price of regular commercial service to the school or library or to the competitively bid price offered by the "service provider" prior to the application of any state provided support for the school or library (13 FCC Rcd at para. 195-6). The USTA objected, arguing that this model permits applicants to receive universal support for state support components, but the Commission found their argument

without merit. ITS acknowledges this conclusion and agrees with the Commission. From the foregoing, ITS submits that our STN costs should be permissible as part of the price bid, when participating schools or libraries compare pricing from ITS, as the STN, and pricing from service providers when determining their source of telecommunications.

A. Appeals

1. Appeals Procedure

Paragraphs 49-52. ITS strongly supports the Commission's willingness to entertain the appeal extension and the postmark date as the filing date. Our experience is that applicants and have been frustrated by the streamlined 30-day appeal window because they often lack telecommunications or legal expertise. Non-substantive appeals only burden the program, artificially escalating administrative costs. As a STN, ITS has filed many appeals associated arising from simple clerical errors in the Administrator's processing. Through participation in the CCSSO, ITS has learned that it is often necessary to file appeals to maintain applicants' rights, while time to research the issue and understand the context is used to ascertain all relevant details. Lengthening the appeals filing period should reduce the number of appeals.

In addition, since almost every other E-rate deadline has been based on the postmarked date, such as the filing deadlines for the Form 470 and the Form 471, some applicants have been confused about the differing deadlines for appeals. ITS supports these changes.

2. How should the Commission fund successful appeals?

In Paragraph's 53-57, the Commission requests comment on how successful appeals should be funded. Present practice establishes a reserve from the annual funding to accommodate successful appeals. ITS shares the Commission's apparent concern that a reserve may not meet the actual number of reversed decisions, possibly rendering the reserve inadequate. A reserve may be the best, if not the only, or most reasonable method of accommodating appeals. If an appeal is denied, thereby releasing the funds, such funds should not, however, be designated as "unused funds". Any such funds should be added to the year then current and disbursed in accordance with the demand, unless a prior funding year remains open.

Appeals are a mechanism for applicants to correct misunderstandings or mistakes made by the Administrator in the application process. The process can also clarify issues not considered in the Commission's regulation or the Administrator's policy. Successful appeals have led to significant changes and improvements in the program, including decisions regarding Copan, Tennessee, Iowa, Williamsburg-James City, Naperville and MasterMind to name a few.

Applicants should not be penalized for misunderstandings or mistakes committed by the Administrator. It is important to fund successful appeals immediately. Funds should be set aside for pending appeals during the funding year. As an alternative to the above, should successful appeal demands exceed the supply of set-aside funds, carryover funds from previous years should fund appeals. If carryover funds are exhausted or non-existent, any funds made available through the Form 500 process should be made available for successful appeals. Do not use subsequent years funding for successful appeals.

IV. Conclusion

ITS reiterates its appreciation for the support the Commission has provided to the Universal Service Program for Schools and Libraries. The Commission has provided leadership and we find the SLD staff helpful and responsive. As shown herein, STNs such as ITS have a significant ability to provide savings to their school and library clients, thereby broadening the reach of the program. We stand ready to assist the Commission on these and other issues as the program moves forward.